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Surviving the *Personal Property Securities Act 2009* (Cth)

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1. Introduction

Australia has new national legislation - the *Personal Property Securities Act 2009* (Cth)¹ and the *Personal Property Securities Regulations 2010* – which is expected to commence operating in February 2012.

Previous personal property securities legislation was very complex, with more than seventy pieces of legislation in the states and territories, and more than forty registers. This reform package is the culmination of a process that began many years ago and various drafts have been the subject of much investigation and consultation. This legislation rationalises previous laws and bring about substantial changes to this area of law. This paper seeks to explain the principal changes and their implications.

The policy objectives of the new legislation are to increase certainty and consistency and to reduce complexity and cost. To achieve this, the legislation will treat like transactions alike, by focusing on substance over form, and so will remove distinctions between security interests which have been based on their structure. Differences based on the location or nature of the secured property and the debtor's legal form, of individual or company, will also disappear. We will have one single national scheme and one national electronic registration system for all security interests throughout Australia. The Act will apply to security interests in tangible and intangible personal property, including those based on some form of title retention which are not security interests under the general law.

2. Application of the legislation

Functional approach to security interests

The traditional forms of security – mortgage, charge, pledge, lien - were adequate for many centuries. But in recent times new forms of security have been developed, designed to let the debtor have possession of the goods to use in his/her business. These new securities are based on the lender's retaining ownership of the goods and letting the borrower have possession.

These take three main forms:

- Conditional sale – ownership does not pass until the buyer or borrower pays for the goods.
- Lease of goods (bailment) of equipment used in the business.

¹ The Act has been amended: *Personal Property Securities (Consequential Amendments) Act 2009* (Cth); *Personal Property Securities (Corporations and other Amendments) Act 2010* (Cth); *Personal Property Securities (Corporations and other Amendments) Act 2011* (Cth). Further amendments are proposed: *Personal Property Securities Amendment (Registration Commencement) Bill 2011*.

- Floor plan/ Display plan (consignment of goods) for inventory which is an agency relationship or a contract for “sale or return” or sale “on approval.”²

A contract “for sale or return” or for sale “on approval” may be made between a supplier of goods and a retail dealer. Such a contract does not pass property rights in the goods when it is made.³ The financier retains ownership while the dealer has the right to buy the goods.⁴ The parties may agree that property is not to pass until the financier receives payment: *Sale of Goods Act 1896* (Qld) s 20 either expressly or by providing that the goods must be “settled for or charged.”⁵ If they do, the financier will retain ownership despite the dealer’s selling the goods to a third party.⁶

These transactions do not create security interests under the general law.⁷ They open up the potential for fraud because third parties dealing with a business are unlikely to know whether stock or equipment is owned by others. The possessor might take another loan on the security of the goods or sell the goods and third parties who did not know about the private security arrangements could be defrauded.

The PPSA regulates these on the basis that an interest in personal property should be a security interest if, because of an arrangement between the parties, one of the parties has a right to take possession of or otherwise deal with the property if the other defaults in performing the obligation owed. The Act does this in three ways:

- First, it defines “security interest” to mean an interest “provided for by a transaction that, in substance, secures payment or performance of an obligation (without regard to the form of the transaction or the identity of the person who has title to the property): s12 (1).
- Second, s 12 (2) provides that certain transactions create security interests if the transaction, in substance, secures payment or performance of an obligation. These include possessory financing arrangements such as a conditional sale agreement (including an agreement to sell subject to retention of title), a hire purchase agreement, a trust receipt, a consignment (whether or not a commercial consignment) and a lease of goods (whether or not a PPS lease).
- Third, s 12 (3) deems what would at common law have been ownership rights to be security interests. They include the interest of a consignor under a commercial consignment and the interest of a lessor or bailor under a PPS lease.

² A contract “for sale or return” or for sale “on approval” does not pass property rights in the goods when it is made: *Kirkham v Attenborough* [1897] 1 QB 201. The financier retains ownership and the dealer has the right to buy the goods: KCT Sutton *Sales and Consumer Law* Fourth Edition LBC information Services 1995 para [14.17]. The parties may agree that property is not to pass until the financier receives payment: *Sale of Goods Act 1896* (Qld) s 20 either expressly or by providing that the goods must be “settled for or charged”: *Weiner v Gill* [1906] 2 KB 574. If they do, the financier will retain ownership despite the dealer’s selling the goods to a third party. KCT Sutton *Sales and Consumer Law* Fourth Edition LBC information Services 1995 para [14.17].

³ *Kirkham v Attenborough* [1897] 1 QB 201.

⁴ KCT Sutton *Sales and Consumer Law* Fourth Edition LBC information Services 1995 para [14.17].

⁵ *Weiner v Gill* [1906] 2 KB 574.

⁶ KCT Sutton *Sales and Consumer Law* Fourth Edition LBC information Services 1995 para [14.17].

⁷ because no property interest has “passed out” of the lessee; the lessee had not “given” anything to the lessor: EI Sykes and S Walker *The Law of Securities* 5th edition 1993 p 5.

A commercial consignment is defined so that it includes most common stock in trade or inventory financing methods where wholesalers provide goods to retailers on display or floor plan financing, but excludes agency relationships where the agency is apparent to others: s 10.

A “PPS lease” is a lease or bailment of serial numbered goods for 90 days or more, or of other goods for at least a year or for an indefinite term, by a lessor/bailor who is regularly engaged in the business of leasing/bailing goods where the bailee provides value: s 13. Motor vehicles, watercraft and aircraft are goods which have identifying numbers and so can be described by their serial numbers.⁸

The legislature has made a policy choice to define PPS leases by their term. These include finance and operating leases. The legislature is interested in regulating commercial consignments and leases because the arrangement gives the appearance that the possessor is the owner and so may deceive other lenders into lending on the security of the stock, or third party buyers into believing the possessor is selling its own goods.⁹

Crucially, s 12 (3) deems transactions which are designed to give the benefits of possession, without the possessor having to borrow money to obtain the goods, to be security transactions and to create security interests. This is a change from common law rules relating to personal property where only an owner can create a security interest in property; under the *PPSA*, a person who has only a possessory interest can do this: s 19(5).¹⁰

The effect then is that it no longer matters whether a security interest is a mortgage, a charge or a trust. The Act does not abolish traditional forms of security but makes the distinctions between them redundant. From now on, a debtor can just grant “security” and it is not necessary to mortgage, charge or assign property.

Security interests not covered by the Act

S 8 provides that the Act does not apply to some security interests or has limited application to them. These include: a lien or charge created under the general law and this would include a solicitor’s lien: (1) (c); statutory water licences : (1) (i); an interest in a fixture: (1)(j); and security interests taken by licensed pawnbrokers over property and for debts of no more than \$5000: (1) (ja), (6). A banker’s right to set-off or combine accounts is excluded: (1) (d) but an ADI may take a security interest in an ADI account that is kept with the ADI: s 12 (4)(b).

Debtors covered

The *PPSA* applies to security interests given by individuals and to corporations and other legal entities such as partnerships. The grantor of the security interest will be the

⁸ *Personal Property Securities Regulations 2010* Schedule 1 Part 2 s2.2 (1) (a), (b), (c).

⁹ The priority and “taking free” rules apply to deemed security interests but they are not subject to the vesting rule (s 268) or to the enforcement rules (s109).

¹⁰ *Graham v Portacom New Zealand* [2004] 2 NZLR 528 where a lessee of portable buildings was held to have sufficient rights to have created a security interest in the buildings.

debtor or a third party guarantor who is granting a security interest to secure a loan to the debtor.

Categories of collateral

Collateral is the personal property over which the security interest is granted: s10. It is divided into a number of categories including inventory, consumer property and commercial property.

3. Enforceability of Security Interests

The Act confirms that parties may make any kind of security agreement they like: s 18.

Creation of the interest- attachment.

Attachment is the term that describes the successful creation of the security interest. A security interest attaches when all the events necessary for the creation of the security interest has taken place, so the grantor has to have rights in the collateral or the ability to transfer rights to the secured party and the secured party must give value: s 19(2). A security interest is only enforceable against a grantor if it has attached to collateral: 19(1).

Perfection

A security interest is enforceable against a third party only if the security interest has attached to the personal property and the secured party has perfected it by control, or taken possession, or there is an agreement in writing signed by the grantor which complies with s 20 (2). The requirements include a statement that a security interest is taken in all the grantor's present and after-acquired property or all except for specified items or classes or describes the collateral (as consumer or commercial property, together with the item or class of property or as inventory): s 20 (2)(b), (4) – (6).

Perfection is important in protecting a security interest from third parties and to preserve the interest if the grantor becomes insolvent. When a security interest is perfected, the secured party has done all it can to protect its interest from competing parties. Perfection requires possession or control¹¹ of the collateral as against the grantor (Part 2.3 *PPSA*) or a registration which is “effective with respect to the collateral”: s21.

Although under the Torrens system, an interest must be created before it can be registered, under the *PPSA*, attachment and perfection can occur in any order: s 21 (3) and a security interest may be registered before a security agreement is made or a security interest attaches to the property: s 161. This means that a secured party can perfect their interest before it attaches to the collateral, thus ensuring it is available for search in the register, although the security interest would not be enforceable against a third party until after attachment to the personal property and the requirements of s 20 had been satisfied. This gives an advantage in a priority dispute.

Time limits for registration of some particular security interests

There are time limits for registration of some particular security interests – these are *PMSI*'s and *SI*'s created by a corporation.

¹¹ Control is available only for certain property: s 21 (2) (c).

The Act has introduced to Australia the concept of purchase money security interests (PMSIs), which are security interests obtained by a secured party who provides a grantor with particular collateral, or funds with which to acquire particular collateral, in contrast to more broad financing such as an overdraft facility. The term is defined to include the interest of a lessor or bailor under a PPS lease and the interest of a consignor under a commercial consignment (s14). A conditional sale also comes within the definition of a PMSI (s 14).

To preserve its priority, registration of a PMSI over inventory¹² or its proceeds must occur:

- (a) if the inventory is goods, by the time the grantor obtains possession of the goods;
- (b) for any other kind of inventory, by the time the PMSI attaches to the inventory: s 62 (2); and

registration of a PMSI over property or its proceeds other than inventory must occur:

- (a) if the property is goods, by 15 business days after the grantor obtains possession of the goods;
- (b) for any other property, kind of inventory, by 15 business days after the time the PMSI attaches to the property: s 62 (3).

From the commencement time of the PPSA, the *Corporations Act 2001* (Cth) will include Pt 5.7B, Divs 2A and 2B which enact particular requirements for security interests granted by a company.¹³ Division 2A provides for the vesting of PPSA security interests if they are not continuously perfected. The principal provision is s588FL which deals with the time of registration of a PPSA security interest. It provides that where a company is wound up, an administrator of a company is appointed, or a company executes a deed of arrangement, a PPSA security interest granted by the company which is enforceable against third parties and perfected by registration on the PPS Register, vests in the company if it was registered after the latest of six months before the critical time (the day the winding up order is made, the day a resolution for winding up is passed or the day the administration began), 20 business days after the security agreement came into effect, or an extended time ordered by a court under s 588FM. This does not apply to deemed security interests (s588FN). Thus a secured party will not be able to retain a security interest granted by a company if the secured party does not register within the later of 6 months before the company becomes insolvent, 20 business days after it was created or an extended time ordered by a court, and maintain the registration.

¹² S 10 defines “*inventory*” to mean personal property (whether goods or intangible property) that, in the course or furtherance, to any degree, of an enterprise to which an ABN has been allocated:

- (a) is held by the person for sale or lease, or has been leased by the person as lessor; or
- (b) is held by the person to be provided under a contract for services, or has been so provided; or
- (c) is held by the person as raw materials or as work in progress; or
- (d) is held, used or consumed by the person, as materials.

¹³ Inserted by the *Personal Property Securities (Corporations and other Amendments) Act 2010* (Cth), Pt 9.

Perfection crucial for preservation

Although registration is not essential for enforceability against third parties, as against a 3rd party buyer of the collateral or a competing security interest holder with whom there is a priority dispute, the secured party may lose the security interest if it is not perfected. Perfection does not mean an interest will prevail against a 3rd party; although necessary, it may be insufficient on its own to achieve this result. Whether that occurs depends on other rules.¹⁴ Perfection is also important for protecting the security interest from a trustee in bankruptcy or liquidator on the grantor's insolvency, as a security interest which is unperfected at the time a grantor becomes insolvent, vests in the grantor: s 267(2).¹⁵ This means that unperfected interests will be considered to be part of the grantor's estate and therefore available for distribution in the grantor's insolvency. This applies even if the secured party had retained title under a lease, hire purchase or conditional sale arrangement.¹⁶

4. The register

Chapter 5 of the Act deals with the establishment of the register, the process for registration, amendment and removal of registrations, and defects in registrations.

The Act establishes a single national online register, known as the Personal Property Securities Register (s147). This will replace approximately forty existing electronic and paper-based State and Territory registers. The Register is electronic and will be accessible 24/7. Although registration is not the only method of perfecting a security interest, it is expected to be the most common.

An on-line notice board¹⁷

Registration enables secured parties to give notice to others dealing with the possessor of the property that the secured party has a security interest in it. But the PPSA makes clear that the fact that a security interest is registered does not give others actual or constructive notice of it: s 300.

Notice filing rather than transaction filing

Notice is given by the recording of data about secured parties, grantors and collateral. A financing statement is registered (ss10, 150), not the security agreement, so the register does not contain detailed information about the transaction between the grantor and secured party. Collateral must be described as "consumer property" or "commercial property": s 153.

Accuracy of data

The PPS provides a system for verifying data recorded on Register which gives grantors an opportunity to check the accuracy of what has been recorded against them: ss155-158. The Act enables secured parties to amend registrations: ss 150(2),

¹⁴ The rules in Part 2.5 for buyers and in Part 2.6 for priorities.

¹⁵ There are exceptions for a PPS lease of property that may or must be described by serial number which is for a term of between 90 days and 1 year and for a commercial consignment, as long as these transactions do not secure payment or performance of an obligation: s 268(1) (ii), (iii).

¹⁶ PPS Bill Revised Commentary para 11.47.

¹⁷ J. O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [15.110]

(3), 153,154, and the Registrar is given power to amend registrations, correct errors and remove data: Part 5.7. There is a process for having outdated registrations removed from the register: s167.

Effective Registration

The Act uses the term “effective registration.” This means the secured party has a financing statement validly recorded on the register.¹⁸ It is crucial to perfection, as s21 provides that a security interest in particular collateral is perfected if a registration is “effective” with respect to the collateral.

Seriously misleading defects make the registration ineffective: s 164. The test of whether a defect is seriously misleading will be objective.¹⁹ Defects specified in s 165 make the registration ineffective if they are the fault of the secured party: s 164(1) (b), s 166 (1) (b). The s 165 defects are:

- where collateral is required to be described by serial number and a search by reference to the serial number does not disclose the registration;
- where collateral is not required to be described by serial number and a search by reference to the grantor’s details does not disclose the registration; and
- an indication that a security interest is a PMSI where it is not: s 165.

The first two of these are related to the ability of a searcher to find the security interest by searching the register. If these defects occur for a reason other than a mistake in a financing statement, then the registration remains effective from the time the defect occurs until the earliest of three possible times²⁰ after which it becomes ineffective.²¹ This provides a grace period for secured parties to correct registrations where events beyond their control have led to a previously effective registration becoming ineffective.²²

Searching the register

The availability of reliable, low-cost, fast and accessible search facilities is a central feature of the PPS system.²³ This enables lenders to find out whether particular property is subject to a current or prospective security interest and allow prospective buyers to learn whether the property they are considering purchasing is free of a security interest.²⁴ Secured parties need to be able to search to verify the validity and history of their own registrations and grantors need to monitor registrations against their property.²⁵

At the same time, there are detailed provisions in the Act to deter parties from making unauthorised searches of the register: ss 172- 174.

¹⁸ Replacement Explanatory Memorandum to PPS Bill para 5.67.

¹⁹ s 164(2); Replacement Explanatory Memorandum to PPS Bill paras 5.70, 5.71. The example given is an incomplete or inaccurate collateral description.

²⁰ s 166 (2) - the end time of the registration, the end of 60 months after the defect time or five business days after the secured party acquires actual or constructive knowledge of the defect.

²¹ The example given is if the grantor’s name changed after marriage: Replacement Explanatory Memorandum to PPS Bill para 5.74.

²² Replacement Explanatory Memorandum to PPS Bill para 5.76.

²³ Replacement Explanatory Memorandum to PPS Bill para 5.84.

²⁴ J O’Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [15.7010].

²⁵ J O’Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [15.7010].

5. Taking personal property free of security interest - The rules benefiting 3rd party buyers

When a grantor of personal property to which a security interest has attached, sells that property, the basic rule is that the security interest continues in that collateral, unless the secured party expressly or impliedly authorised the sale, and attaches to the proceeds, unless the security agreement provides otherwise: s 32. This means that if the sale is a breach of the security agreement, the security holder's rights continue and the buyer takes subject to the security interest, by application of the common law rule of *nemo dat quod non habet*.

To have a sustainable workable system, the Act needed to promote ease and speed in commercial transactions, and preserve buyer confidence in the retail market. For these reasons, the *PPSA* includes rules which safeguard consumers from sellers who hold property subject to secured interests but seek to sell it on the basis that it is unencumbered. The legislature has had to strike a balance between protecting the interests of security holders against the need to protect innocent buyers. The scheme aims to match consumer expectations with business needs.

The rationale of these provisions is that a secured party should perfect their security interest. If they do not, a buyer will ordinarily take free of that interest. But even if the secured party does perfect their security interest, in some circumstances, a buyer may still take free of the interest. There is no concept of a "buyer in good faith" in the *PPSA*.

If a buyer comes within any one of the rules which lets a buyer take free of the security interest, that is enough for the buyer to succeed.²⁶

Unperfected security interests

A buyer or lessee for value takes the personal property free of an unperfected security interest in the property, unless the transferee was a party to the transaction that created or provided for the security interest: s 43. This is the case, even if the buyer or lessee knows of the interest.

This provision gives secured parties a strong incentive to register. The approach is that the secured party is in the position of being able most easily to reduce the risk of loss and should have done something to give notice.

Rules for perfected security interests

Even if the owner registers the security interest the policy choice has been made that in a number of circumstances, if the grantor sells or leases the secured property, the buyer/lessee takes free of the security interest.

²⁶ PPS Bill Revised Commentary para 5.4 December 2008

These rules apply to goods.²⁷ An exception common to them is that they do not benefit third party buyers or lessees who take the goods as inventory.²⁸ So a dealer would not take free of a security interest under these rules.

- *Incorrect or missing serial numbers*

This is concerned with sales of personal property that may²⁹ or must³⁰ be described by serial number³¹ in a registration. S 44 provides that a buyer or lessee takes free of the security interest if a search of the register, immediately before the time of the sale, by reference to the serial number, would not disclose a registration that perfected the security interest, unless the transferee was a party to the transaction that created or provided for the security interest.

The effect is that registration against the grantor's name will not protect the security interest. It does not matter if the buyer did not actually search the register by reference to the serial number.

The Regulations provide that aircraft, motor vehicles or watercraft, if described as consumer property in the register, are required to be described by serial number;³² but if they are described as commercial property in the register, they "may" be described by serial number.³³ Goods which are required to be described by serial number in the register must be registered that way for the registration of the security interest to be effective: ss 164,165. If a registration is not effective, the security interest is unperfected: ss 21(2) (a), 164(1).

Therefore there is no scope for the operation of s44 with regard to serial numbered consumer goods, because, if a search of the register by reference to serial number only would not disclose the registration, the registration would not be effective and a buyer or lessee would take free of the unperfected security interest under s 43.

The impact of s 44 is on serial numbered commercial property. Its effect is that, although lenders with security interests over commercial aircraft, motor vehicles or watercraft do not have to register on the serial number index to make the registration effective under ss 21 and 164, if they register against the grantor's name rather than by reference to the serial number of the goods they risk a buyer being able to take free of the security interest under this provision. This will be the case unless the buyer is

²⁷ Other rules apply to currency: s 48; investment instruments and interests in an intermediated security: ss 49, 50, 51.

²⁸ ss 44(2) (a); 45(2) (c); 45(4) (c); s 46 (2) (a). Inventory is personal property held for use in a business: s 10.

²⁹ aircraft, motor vehicles or watercraft if described as commercial property in the register, may be described by serial number: Regulations Part 3 s 3.2 (1) (b).

³⁰ aircraft, motor vehicles or watercraft, if described as consumer property in the register, must be described by serial number: Regulations Part 3 s 3.2 (1) (a).

³¹ For motor vehicles, this is the identification number, chassis number or manufacturer's number: Regulations Part 3 s 3.2 (2) (c).

³² *Personal Property Securities Regulations 2010* Schedule 1 Part 2 s2.2 (1) (a).

³³ *Personal Property Securities Regulations 2010* Schedule 1 Part 2 s2.2 (1) (b), (c).

a dealer in the property, due to the exception against taking inventory free of security interests.³⁴

- *Motor vehicle purchases or leases and incorrect or missing serial numbers*
(the day and a half rule)

A buyer or lessee, for new value,³⁵ of a motor vehicle³⁶ takes free of a security interest if there is a time during the period between the start of the previous day and the time of the sale or lease when a search of the register by reference only to the serial number³⁷ of the motor vehicle would not disclose a registration that perfected the security interest: s45 (1), (2). Exceptions include the transferee taking with actual or constructive notice of the security interest: s 45(2) (d).

Again, this provision will not apply to sales or leases of consumer property³⁸ because, to be effective, registration must be under the serial number; if the serial number is missing or incorrect, the registration is ineffective and the security interest is unperfected. It will apply only to commercial property.³⁹ Secured parties lending on commercial property can protect themselves from the operation of this provision by registering correct serial numbers, and by registering their security interest prior to the security interest attaching to the goods.⁴⁰

- *Motor vehicle purchases or leases from dealers or traders*

S 45 (3) and (4) apply to prescribed motor vehicle dealers and traders.⁴¹ A buyer or lessee for new value takes a vehicle from such a dealer free of a security interest unless they have actual or constructive knowledge that the transfer is a breach of the security agreement that provides for the interest.

This exception makes clear that those who buy from licensed dealers do not have to search the register before buying. This policy choice is designed to facilitate sales by dealers, so financiers who lend to dealers run the risk of losing their interest, whether or not they register it.

- *Transactions in the ordinary course of business*

A buyer or lessee takes personal property free of a security interest given by the seller or lessor or that arises under s 32 (proceeds) if the personal property was sold or leased in the ordinary course of the seller's or lessor's business of selling or leasing

³⁴ Replacement Explanatory Memorandum to PPS Bill para 2.80.

³⁵ **new value** means value other than value provided to reduce or discharge an earlier debt or liability owed to the person providing the value: s10.

³⁶ prescribed and defined in Regulations 1.7 and 2.1.

³⁷ Security interests in motor vehicles require registration against the serial number if the financing statement describes them as consumer property and may be registered against the serial number if described as commercial property: Regulations Part 3 s 3.2 (1) (a) and (b).

³⁸ s 10 *consumer property* means personal property held by an individual, other than personal property held in the course or furtherance, to any degree, of carrying on an enterprise to which an ABN has been allocated.

³⁹ s 10 *commercial property* means personal property other than consumer property

⁴⁰ ss 21 (3), 161 PPSA.

⁴¹ Regulation 2.2 prescribes dealers and traders who hold a license issued by State or Territory licensing authority.

personal property of that kind, unless they have actual knowledge that the transfer is a breach of the security agreement that provides for the interest: s 46.

The rationale of this provision is that an informed buyer might expect that a trader has created some security interest over its stock but might also expect that the security agreement would allow the trader to sell its stock in the ordinary way.⁴² The object is to promote certainty and confidence in the commercial market.⁴³ So again the legislature has made a policy choice to facilitate transactions in the ordinary course of business – it would be too disruptive for buyers to have to search the PPS register before buying from a retailer.

- *Low Value Consumer Property.*

A buyer or lessee for new value of personal property that the buyer or lessee intends to use predominantly for personal, domestic or household purposes takes the personal property free of a security interest in the property, if the market value (worked out at the time each part of the total new value is given) of the total new value given for the personal property is not more than \$5000 or a greater amount prescribed by the Regulations:⁴⁴ s 47.

There are three exceptions where the buyer or lessee will not take free of the security interest. First, if the personal property may or must be described by its serial number in the registration – aircraft, watercraft⁴⁵ and motor vehicles.⁴⁶ Second, if the buyer or lessee takes the goods with actual or constructive knowledge that the sale or lease constitutes a breach of the security agreement that provides for the security interest. Third, at the time the sale or lease agreement is entered into, the buyer or lessee believes and it is actually the case, that the market value of the goods is more than \$5000 or a greater amount prescribed by the Regulations.⁴⁷

This rule applies whether or not the disposition is in the ordinary course of business of the seller/lessor⁴⁸ and to private sales.

Effect of the operation of these rules

The rules in Part 2.5 of the Act allow a buyer to take free of a security interest but do not extinguish the interest. It attaches to the proceeds, unless the security agreement provides otherwise: s32 (1) (b). As well, the secured party obtains subrogation rights to the transferor's rights to the purchase price: s 53. On either basis, the secured party

⁴² J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [30.1510]

⁴³ J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [30.1510].

⁴⁴ No greater amount has yet been prescribed by the Regulations.

⁴⁵ Aircraft and watercraft are defined in Regulations 1.6.

⁴⁶ Defined in Regulation 1.7.

⁴⁷ No greater amount has yet been prescribed by the Regulations.

⁴⁸ J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [30.2010].

is entitled to be paid the debt in respect of which the security interest was taken or the value of property it owned.⁴⁹

6. Priority rules

Part 2.6 of the Act sets out detailed rules dealing with priorities.

Secured parties may agree on the order of priority of their interests: s 61. If they do not, the Act provides special priority rules to govern certain security interests, and then default priority rules.

Purchase Money Security Interests

The most significant special priority rules are for Purchase Money Security Interests (PMSI's). If a grantor has collateral already subject to security interests, and seeks further finance to acquire a specific chattel, a lender is more likely to lend for that purpose if the lender can obtain a security interest over that asset. Thus PMSI's enable a grantor to acquire further collateral. A PMSI gives a holder super-priority over all other security interests, even those perfected earlier, except for security interests perfected by control: s 57. This special priority does not prejudice existing secured creditors because a PMSI cannot extend to other collateral and the new collateral is the result of a new loan. The rules are designed to give practical assistance to businesses to obtain financing for specific purchases they may need to increase productivity.

PMSI's are commonly created as a result of a loan for a specific purpose. There must be a direct connection between the money provided and the goods bought with that credit. A retention of title arrangement, a loan to purchase specific goods, a PPS lease (a finance lease with a life of at least one year) and a commercial consignment, are all PMSI's: s 14.

Super-priority Rules:

1. PMSI v other perfected security interests

A perfected PMSI has priority over another perfected security interest that is not a PMSI if it is registered within the times required and the registration states that it is a PMSI: s 62 (2), (3).

2. Priority between PMSI's

A perfected PMSI of a seller, lessor or consignor of collateral or its proceeds has priority over other PMSI's of other lenders, as long as that priority interest is perfected by a particular time: s 63.⁵⁰

Default priority rules

1. A security interest perfected by control has priority over a security interest in the same collateral perfected by other means: s 57.

2. A perfected security interest has priority over an unperfected security interest: s 55 (3).

⁴⁹ For further detail about the rules and their relationship with the Sale of Goods legislative exceptions to the *nemo dat* rule, see D. McGill "Transfer of title by a Non-owner: The Personal Property Securities Act 2009 (Cth) exceptions to the *nemo dat* rule" (2011) 39 ABLR 209.

⁵⁰ This is subject to s 57 (perfection by control).

3. Priority between two perfected interests is determined by the earliest time of registration, the time of perfection by taking possession or control, or the time of temporary perfection: s 55 (4),(5).

4. Priority between unperfected interests is determined by the order of their attachment: s 55(2)

These rules apply so that a party who once would have been able to rely on their ownership rights to property, whether by retention of title through a conditional sale, or by leasing or consigning the property for sale, may be defeated by a subsequent security holder who perfects their security interest first, even if that subsequent security holder knew of their interest.

7. Enforcement

Chapter 4 of the Act deals with enforcement. These rules do not apply to the transactions that are deemed to have given rise to security interests in s12 (3): s 109(1). This is because these are not security interests - they do not secure the payment or performance of an obligation - and so should not be subject to security interest enforcement remedies.⁵¹

There are a number of guiding principles. First, the Act does not derogate from the rights and remedies the grantor and secured party have against each other under their agreement: s 110, so the PPS is not a code for the enforcement of security interests.⁵² The result is that the parties will continue to have their rights under the security agreement, under any other relevant legislation and under the common law or equity.⁵³ Second, the rights and remedies provided are cumulative: s114. Third, it is not necessary for the secured party to obtain a judgment before exercising its rights and remedies: s113. Fourth, parties may contract out of enforcement provisions in relation to collateral used for business purposes: s115.

The overriding duty on a secured party in enforcing a security interest is to act honestly and in a “commercially reasonable manner”: s 111. This duty to act in a “commercially reasonable manner” has no express counterpart in general law or other statutes. The purpose is to ensure fairness to the debtor and any guarantors of the debt in any remaining equity in the collateral and to any other secured party whose security interest has lower priority.⁵⁴ A secured party who fails to discharge any of its statutory duties, can be liable for loss or damage to the person to whom the duties are owed and any other person who can reasonably be expected to rely on the performance of the duties: s 271.

Chapter 4 provides secured parties with the following rights and remedies:

- a right to seize collateral by taking physical possession or steps to gain control of the collateral, subject to protection for parties with higher priority: ss 123-127;

⁵¹ Replacement Explanatory Memorandum to PPS Bill para 4.5.

⁵² J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [45.510].

⁵³ J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [45.510].

⁵⁴ J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [45.510].

- a right to dispose of the seized collateral (s 128), subject to certain conditions regarding notice (s 130) and duties regarding the sale price (s 131) and accounting for proceeds (s 132);
- a right to defer the sale of collateral: s 125 (3);
- a right to buy collateral that is not used predominantly for personal domestic or household purposes, in certain circumstances and subject to certain conditions: ss 109(5), 129;
- a right of foreclosure in relation to retained collateral, subject to certain conditions in relation to giving notices to interested parties: ss 134 -138.

Enforcing mortgages of land and personal property – relationship with land laws.

If the same obligations are secured by a mortgage of land and a security interest in personal property, the secured party may choose to enforce the security interest in personal property in the same way as the interest in the land may be enforced under the land law: s117. The modern mortgage debenture usually creates a fixed charge over land and plant and equipment and a floating charge over all other assets of company. From now on, the holder of the mortgage debenture need not initiate separate proceedings against the land and the personal property to recover its secured debt. Instead a choice is available between enforcing against the personal property under Chapter 4 of the PPSA and enforcing against the personal property as if it were land. This will reduce costs and promote efficiency in the enforcement process.⁵⁵ In choosing between these remedies, the secured party must make the decision reasonably and take into account certain matters: s 117 (3).

Relationship with National Credit Code

Chapter 4 applies to a security interest in collateral to which the National Credit Code applies: s119. Compliance with a provision of the NCC amounts to compliance with the corresponding provision of Chapter 4: s 119(2) and PPS Regulations 4.1.

8. Conclusion

The legislation rationalises the law to reflect the realities of modern personal property financing. It prevents secured parties from structuring transactions to rely on their retention of title which in the past allowed possessors to create false impressions of liquidity which have deceived many buyers and creditors. The comprehensive legislation appears to have managed its relationships with other relevant legislation to minimise costs and streamline processes as far as possible.

⁵⁵ J O'Donovan *Personal Property Securities* Legal Online Commentaries Thomson Reuters (Professional) Australia [45.2010].